M87/989

FET

Foreign Economic Trends and Their Implications for the United States

MAY 1989

MOZAMBIQUE

FET 89-51
Frequency: Annual
Supersedes: 88-55

PREPARED BY
AMERICAN EMBASSY MAPUTO

U.S. DEPARTMENT OF COMMERCE
International Trade Administration
Washington, D.C. 20230

Available by subscription from the Superintendent of Documents, GPO, Washington, D.C. 20402. Annual subscription, $55.00. Foreign mailing $13.75 additional. Single copies, $1.00, available from Publications Sales Branch, Room 1617, U.S. Department of Commerce, Washington, D.C. 20230.

C 61.11:

READEX FICHE best copy available

KEY ECONOMIC INDICATORS

(In Millions of U.S. Dollars Unless Otherwise Noted)

Domestic Economy	1985	1986	1987	1988 (unaudited)
Population (millions)	13.8	14.2	14.5	14.9
Population growth (%)	2.6	2.6	2.6	2.6
GDP	3,395.1	4,129.1	1,505.6	1,565.8
Per Capita GDP	246.0	290.8	103.8	105.1
GDP Index (1985)% Change	-0.0-	0.6	4.0	5.0
GSP Index (1985)% Change	-0.0-	10.7	173.6	5.0
Consumer Price Index % Chg	29.2	38.9	163.3	83.1
Production and Employment				
Labor Force (thousands)	6,638.0	6,815.0	6,995.0	7,100.0
Unemployment (Avg. %)	20.0	25.0	35.0	40.0
Indus. Product % Change	-23.6	-4.2	5.7	5.1
Oper. Deficit, % GDP	3.4	12.1	5.3	4.0
Deficit, pre-grant % GDP	8.0	17.7	21.1	25.0
Balance of Payments				
Exports (F.O.B.)	76.6	79.1	97.0	99.9
Imports (C.I.F.)	423.8	542.7	611.3	764.5
Trade Balance	-347.2	-463.6	-514.3	-664.0
Current Account Balance	-441.1	-622.3	-662.3	-861.0
Capital Account Balance	- 39.7	- 51.5	- 83.0	11.9
Overall Balance	-354.5	-488.0	-436.7	-408.0
Foreign Exchange Reserves	13.9	9.9	80.2	108.0
Avg Exchange Rate (X=US$1)	43.18	40.42	286.67	525.0
Foreign Debt And Investment				
Debt	2,370.0	3,156.7	3,598.4	4,400.0
Debt Service Paid	36.0	59.7	40.2	55.8
Debt Service Owed	103.2	177.0	174.9	177.2
Debt Service Ratio	134.7	223.8	180.3	177.4
Direct Investment (new)	0.36	0.50	0.0	1.3
Direct Investment (cum.)	1,163.06	1,163.56	1,163.56	1,164.86
U.S. Direct Invest. (cum.)	0.36	0.86	0.86	0.85
U.S. Share (%)	0.03	0.07	0.07	0.07
U.S.- Mozambique Trade and Aid				
U.S. Exports to Moz.F.A.S.	55.7	23.4	50.3	56.5
U.S. Imports from Moz.CIF	17.4	20.0	30.1	22.5
U.S. Share Moz.Exports(%)	22.7	25.3	31.0	22.5
U.S. Share Moz.Imports(%)	13.1	4.3	8.2	7.4
U.S. Bilateral Economic Aid	60.4	46.0	65.8	93.0

Principal U.S. exports: food, clothing, parts for transport sector, farm equipment.
Principal U.S. imports: cashews, sugars, shellfish, tea.

Sources: Mozambique Bureau of Statistics, U.S. Department of Commerce.

SUMMARY

During 1988 and early 1989, activity by anti-government forces ("Renamo") seriously affected all provinces. Economic activity remained limited. Mozambique's vast resources remained untapped, as attacks and threats of attack undermined agriculture, inhibited transport, intimidated potential foreign investors, and required costly security for economic infrastructure. As the government struggled to attract foreign capital, the economy remained dependent on foreign assistance.

Economic data for 1987 show improvement of production and worsening of financial status. Gross Social Product grew in volume by 4 percent, but declined in value because of devaluations of the currency. The current account deficit increased by 6.4 percent and was projected to increase by 30 percent to $861 million for 1988. External debt increased from $3.2 to $3.6 billion in 1987 and was projected to increase to $4.4 billion in 1988. Debt service owed, as a percentage of exports, declined from 223.8 percent to 180.3 percent in 1987 and was projected to decline to 177.4 percent in 1988. However, some estimates of exports in 1988 are well below target, and external debt service is undetermined, because the government has not completed its rescheduling agreements with members of the Paris Club.

The Program for Economic Rehabilitation (PRE) continues to reduce centralized control. Fewer goods are restricted to import and export only by parastatal firms. Fewer prices are controlled. Devaluations, withdrawal of food subsidies, and other measures of the PRE have resulted in significant hardship for the population.

Prospective improvement in relations with the Republic of South Africa may facilitate economic cooperation and much needed investment. Mutual interests exist in the transport, energy, and tourism sectors. Joint governmental commissions and private firms are at work to identify feasible projects.

Near-term sales depend entirely on financing for development programs. Long-term markets depend on progress in three areas: physical security, the PRE, and regional economic integration. Prospects for progress could be increased by the growing cooperation with the Republic of South Africa. Profitable investments can be identified, the security situation notwithstanding. The Maputo International Trade Fair is an important opportunity for firms to establish themselves and to reach regional markets.

PART A: CURRENT ECONOMIC SITUATION AND TRENDS

Growth: In 1987, the economy reflected the difficult security situation, an increase in international assistance, and adjustment policies of the Program for Economic Reform. Gross Social Product grew in volume by 4 percent, but declined in value because of devaluations. Three of the five major sectors of the economy--

agriculture, industry, and commerce--showed increases of 6.8, 5.9, and 3.5 percent, respectively. Construction decreased by 16 percent, and the transport and communications sector declined by 4.3 percent.

Preliminary data for 1988 show growth in real GDP of between 4 and 4.6 percent. According to the government, problems in importing raw materials, spare parts, and energy were overcome, and the industrial sector grew by 5.1 percent. The transport sector grew by 4 percent, but agriculture grew by only 2.6 percent, which was the principal reason for the failure to meet the target for overall growth of 6 percent.

Agriculture: In 1987, total production, including crops, forestry products, and livestock, grew by 6.8 percent. Production of cashews, second only to shrimp in value of exports, dropped by 6.5 percent. Tea, another key export, decreased by 71.9 percent to 1,800 tons. Refined sugar increased by 15.5 percent to 19,402 tons.

Six of the 15 commercial products other than cashews and tea showed increases in production during 1987, in the following percentages: cotton (161.1), rice (65.8), corn (27), beans (228.6), beef (17.4), and milk (56.3). Sunflower seed production was unchanged after a drop of 82 percent in 1986, and the percentage decreases in the remaining eight products were as follow: potatoes (69), vegetables (13.4), cocoanut (10.8), citrus (41.6), hemp (80.1), pork (17.6), poultry (33.3), and eggs (61.9). Of the six increases, all except cotton, which increased by 89 percent in 1986, represent modest recoveries from drastic reductions in the range of 30 to 65 percent in 1986. In contrast with these national figures, production in the "Green Zones" of Maputo province has increased steadily because of the assitance received from the Commodity Import Program (CIP) of the U.S. Agency for International Development.

Preliminary data for 1988 indicate overall agricultural growth of 2.6 percent, with commercialized production up by 9.7 percent, both of which results are below targets. Marketed grain was expected to increase from 58.8 to 75 tons, with increases in corn offsetting decreases in rice production. Cotton was expected to decrease from 28,000 to 20,000 tons, and cashews were to increase from 37,500 to 45,000 tons.

Industry: In 1987, total industrial production, including fisheries, grew by 5.9 percent following a decline of 4.2 percent in 1986. Manufacturing increased by 6.8 percent, and energy production increased by 12.5 percent. Construction decreased by 16 percent, with a remarkable shift from state and mixed firms to private firms. This growth ends the decline which began in 1983 and left production at 51 percent of its 1981 value.

Factories and associated transport facilities continue to need rehabilitation. Destruction and neglect limit the productive

capacity of every industry. Lack of foreign exchange for spare parts and raw materials causes plants to operate far below capacity.

Mining: The highest priority of the government's campaign to attract foreign investment is developing extraction of minerals, Mozambique's most valuable resource. Recent explorations have shown promising signs of several strategically important minerals. A survey by the U.S. Trade Development Program in June 1987, resulted in the following estimates of deposits: heavy metals, including ilmenite (titanium), zircao, and monazite (25 million tons); rare earth minerals, including yttrium, beryllium, and tantalum (quantity unknown); strategic minerals, including nickel, cobalt, chromium, platinum, manganese, and graphite (10 million tons of graphite; other quantities unknown); industrial minerals, including diatomite, bentonite, bauxite, and fluospar (1.5 million tons of diatomite; other quantities unknown); energy minerals, including coal (10 billion tons) and natural gas (140 billion cubic meters). Graphite and ilmenite have been identified as prospects for feasibility studies.

In 1987, mineral production rose by 29.9 percent. Coal production increased by 67.5 percent, metallic minerals dropped by 53.8 percent, and gemstones rose by 12.2 percent. Lack of security for rail lines hampers exploitation of all deposits.

Considerable exploration is in progress. The extensive coal deposits in the Moatize region of Tete province, which have long been of interest to the Soviet Union, the German Democratic Republic, Czechoslovakia, and multinational firms such as Lonrho, are now the object of growing interest by Brazil. Transport problems associated with the lack of security have prevented all but token extraction of coal. Several companies are independently exploring for heavy metals on the coast of Zambezia province. Early tests for ilmenite are favorable, and more extensive explorations are likely to begin in mid-1989.

Transport and Communications: Preliminary data for 1988 show an overall growth of 4 percent for the transport sector and a 9.5 percent decline in international rail traffic, which was caused by a 19 percent decline in traffic from the Republic of South Africa. Rail traffic on the Beira Corridor continues to grow, with 1.4 million tons of cargo during January-August 1988, a significant rise from the 1.1 million tons during the corresponding part of 1987. International road and air cargo traffic both decreased by 20.1 percent, while shipping increased by 2.2 percent.

Transport services for neighboring countries are traditionally a main source of foreign earnings. The port-rail systems of Beira, Nacala, and Maputo are vital economic factors. Despite attacks by bandits, improvements on the key rail lines are proceeding. British assistance is critical for rehabilitation of the Limpopo

line to Maputo. The government has received pledges of an additional $30 million from the United Kingdom, Sweden, and the World Bank, and is negotiating an additional $40 million with Japan, Austria, Denmark, Italy, the European Economic Community, and the African Development Bank. The Nacala-Nampula line is being rehabilitated with French, Portuguese, and Canadian assistance.

Transport is high on the list of areas for increased cooperation with the Republic of South Africa. Along with remittances for the labor of Mozambican miners, transport fees are the main benefit from the economic relationship with the Republic of South Africa. A joint committee is reviewing all aspects of road, rail, air, and maritime transport and is emphasizing the task of increasing the use of the Maputo port. A political agreement specifies the responsibility of the Republic of South Africa to increase its traffic through the port, and discussions are beginning on road construction to improve links with Maputo. Meetings to plan cooperation are occurring at all levels between the two governments.

Improvement in the port of Beira is proceeding rapidly. The Beira Port Transport System has a Ten-Year Development Plan with total financial requirements of $661 million for port, railway, telecommunications, road, and other infrastructure projects to attract modern container shipping. The Beira Corridor authority reports that the port can process 30 containers per hour and that this rate is competitive with any port in the region. Modernization of handling berths, storage, and forklifts, and the installation of a 12-kilowatt generator for assured power are impressive changes. The principal concern of the Chief Technical Advisor is that there may not be enough trained personnel to operate the port on completion of the construction. To meet this need, the development plan includes daily training in English, use of computers, and technical skills.

Similar managerial problems are critical in the effort to improve the port of Maputo, the principal users of which are citrus and coal exporters in the Republic of South Africa. The $10 per-ton cost advantage based on mileage alone which Maputo enjoys over Durban for shippers in the Republic of South Africa's eastern Transvaal region is overbalanced by the cost of lost time in port management. Wages are below subsistence, and systematic pilferage is becoming common. The Republic of South Africa has provided $3.75 million for improvement of the coal terminal and personnel for technical assistance. Norwegian donations of $7 million modernized the coastal shipping terminal.

Budget: Deterioration of the government's account continued in 1987. The current deficit, as a percentage of GDP, improved from 12.1 in 1986 to 5.3 in 1987, but investment expenses increased the total deficit from 17.7 to 21.1 percent of GDP during the same period. Defense was the largest expenditure, (46 percent) after a

drop in 1986 (to 29 percent) from its 1985 level (46 percent). Price subsidies were 6.1 percent of total expenses in 1987, compared with 1.3 and 2.1 percent in 1985 and 1986, respectively.

Preliminary data for 1988 show the deficit at 29 percent of current revenue, compared with 26.6, 91.5, and 33.4 percent for the three preceding years. The 1989 budget projects this figure to drop to 21 percent. Revenue is projected to rise by 37.5 percent as the result of increased customs duties and the revision of the tax system. Expenses are projected to increase by 30 percent, with defense taking its present share, about 40 percent. In a measure expected to raise about meticais (MT) 3.75 billion of the MT80 billion needed for defense, the government enacted a new income tax.

Balance of Payments: The external account declined again in 1987, but more slowly than in preceding years. At $97 million, exports were 15.9 percent of imports, compared with 14.6 and 18 percent for the preceding two years. In absolute terms, the trade deficit reached $514.3 million, or a 10.9 percent increase, compared with the 33.5 percent increase in 1986. Imports of food, spare parts, and raw materials overshadowed the substantial increase in exports. A services deficit of $148 million contributed to the largest current account deficit since 1982, $662.6 million.

In 1988, estimated imports and exports both rose by 24 percent. The plan for 1989 contains increases of 22 percent for exports and 10 percent for imports. Essential imports in 1989, with existing credits and donations, are unfunded to the extent of $47 million, which must be found in new donations, increased exports, or debt relief.

Foreign Investment: With a few exceptions, the government's campaign to attract foreign investment has been undercut by the lack of physical security. The few private investors in Mozambique either have other business commitments in the southern African region or are engaged in high-investment areas, such as mineral exploration for which potential profits justify the cost of security. In general, bankers' risk assessments have prevented new investment, in spite of the fact that individual projects are often demonstrably profitable including the cost of security, usually estimated at 12 percent of operating costs. Many multinational firms continue to monitor conditions and to survey various investments with a view toward beginning operations whenever improvements occur in the security situation.

A more subtle barrier to foreign investment is the substantial amount of foreign assistance and associated sales packages being provided to Mozambique by a number of countries. An important feasibility study by a U.S. firm found that competition for the products of the proposed investment would be in the form of donations.

The dominating foreign investment, the Cahora Bassa Dam, is far larger than all others combined and lies dormant, effectively stalemated by the security situation. Designed during the colonial period to provide electricity to the Republic of South Africa, the dam was valued at $550.4 million at the time of independence in 1975, when 81.66 percent was owned by the Government and banks of Portugal and 18.34 percent by the Government of Mozambique. The agreement for operation of the dam originally provided for gradual transfer of shares until Mozambique acquired full ownership in the year 2005, but the transfer has not been implemented. Portugal's share in 1986 is valued at $1.2 billion. Because of the yearly costs of debt service ($50 million) and maintenance ($70 million), not including repair of sabotaged transmission lines, combined with the obvious potential of the dam for regional development, interest in improving the management and distribution capability culminated in April 1988 in an agreement among Mozambique, Portugal, and South Africa. Central to the agreement is the provision for security of the transmission lines, the sabotage of which has raised the cost estimates of the dam by a factor of three.

The level of foreign investment did not change significantly in 1987 or 1988. According to the Chamber of Commerce, there were ten new small investments in the range of $38,000 to $5 million by Swiss, Portuguese, British, South African, and Dutch firms. These investments, mostly in agriculture, are considered first steps to provide footholds for larger operations when the security situation permits. U.S. investment remained at less than $1 million. A U.S. firm successfully spent $1.3 million for mineral exploration in 1988 and will spend at least $2 million for expanded exploration in 1989. These explorations may well form the basis for investment in mineral production on a much larger scale in the target year 1992. U.S. investors already familiar with the region have recently identified opportunities for joint-venture rehabilitation of factories in such areas as soap manufacturing and vegetable oil storage and distribution.

Foreign Debt: The agreement with the Paris Club in June 1987, by which Mozambique rescheduled $407 million and received commitments for $700 million in 1987 and $835 million in 1988, included the requirement that Mozambique conclude agreements with each of its creditors on individual interest rates before June 1988, a requirement which Mozambique did not meet. Instead, the government negotiated concessional interest rates with the creditors who have the largest assistance programs with sales tied to home-country manufacturers and left agreements proposed by Western creditors at market interest rates unsigned. The government stated that survival of the Program for Economic Rehabilitation (PRE) required an average interest rate of 2 percent.

Italy, Portugal, France, Sweden, Norway, and several others forgave large portions of their loans and reduced interest rates on rescheduled amounts. For example, Portugal granted a ten-year grace period, an interest rate of 4 percent for three-quarters of this debt, and conversion of the remaining quarter into equity in jointly owned companies--thus essentially forgiving one quarter of the debt. France plans to forgive one-third of its loans.

Debt management is governed by political forces, which determine the priority of creditors, and secondarily by the long-term economic interests of those creditors as developmental partners with Mozambique. In purely economic terms, there is no possibility that Mozambique could repay its debt as currently estimated. In its strategy for concessional interest rates, the government potentially benefits from the global reconsideration of all aspects of debt in developing countries.

The Economic Rehabilitation Program (PRE) of 1987-89

In courageously pursuing decentralizing policies, the government has begun to create the structural conditions for growth at the cost of significant hardship for the population. Price controls have been removed on almost all but the most basic foodstuffs, and prices which remain controlled have been raised substantially. The two devaluations of 1987 have been followed by four more in 1988 and early 1989. The number of goods permitted for import and export only by parastatal firms has been reduced from 38 to 25. Interest on all bank accounts has been institutionalized, and the management of foreign exchange has been liberalized to allow more individuals to have accounts in convertible currency. These and other, lesser measures have begun to set the stage for increased economic activity.

The cost of these measures, in terms of hardship for the people, is of concern to the government and the World Bank. Price increases associated with the devaluations have left the population with a lack of means to survive. Prices have risen much more than wages. Domestic fuel, bus fares, and electricity have risen 169, 160, and 20 percent, respectively. A new wage scale announced in late 1988 provided a general increase of 15 percent and an increase of 50 percent for the lowest paid workers. Pressure is on the government to reintroduce into the budget food subsidies, thus reversing an important policy of the PRE.

For the PRE to create conditions favorable to private economic activity will evidently require a long time. Having demonstrated beyond any serious question that it is willing to enact policies which liberalize the economy, the government has a formidable challenge in the implementation of those policies. Failure to apply decisions can undercut the effort to create economic growth and to stimulate private business activity. For example, the government can have management problems in carrying through price

increases and permissions to import raw materials directly which it might grant a company. Devaluations can wipe out working capital and parastatal firms might import raw materials at high prices and with surcharges. Even after agreeing to remedy such conditions, the government can have problems in implementation of needed changes. The challenge for the government is to translate the intentions of the PRE into specific actions which support creative economic activity.

PART B: IMPLICATIONS FOR THE UNITED STATES

The Mozambique market contains significant import opportunities. However, most of them are tied to projects funded by international donors in the following sectors: transport, communications, agricultural, and urban improvement. Mozambique's role within the Southern African Development Coordination Conference (SADCC) as the leader of the Southern African Transport and Communications Commission (SATCC), which is located in Maputo, makes it the focal point for regional projects in railroad rehabilitation and telecommunications development. In 1988, USAID provided $13.1 million to support railroad rehabilitation as part of a commitment to provide $34.5 million by 1991. Agricultural projects center on irrigation. Urban improvement efforts include a World Bank loan of $50 million for Maputo and Beira, which is the basis of opportunities for sales related to construction. Projects for regional telecommunications systems are under discussion by international donors. Several U.S. firms have shown interest in various aspects of Mozambique's developmental assistance market.

The strategy for U.S. firms interested in exporting to Mozambique should be: (1) to monitor the programs of international and bilateral assistance organizations such as the International Monetary Fund (IMF), the World Bank, the African Development Bank, and the U.S. Agency for International Development; (2) to monitor changes in international debt rescheduling policies, which profoundly affect Mozambique's economy; and (3) to establish appropriate presences in Mozambique, primarily through the use of representatives and agents. An effective vehicle for the third part of this strategy has been participation in the U.S. commercial exhibit at the Maputo International Trade Fair. In 1989, the fair will celebrate its 25th anniversary and will be the center of extraordinary attention within the region.

Investment opportunities exist for extraction of natural resources and for rehabilitation of factories. Both of these activities are conducive to the taking of profits in resources or products rather than in currency. Numerous opportunities exist to provide capital, machinery, and management for the rehabilitation of wood, soap, glass, furniture, and other factories which have suffered partial destruction or neglect.

The Government of Mozambique is exerting great effort to attract foreign investment for development by creating policies favorable

for profitable enterprises. Applications of the minerals law, the investment code, offshore banking agreements, and the ongoing revision of export regulations are examples of these policies. The attitude of the government is open and supportive.

The Maputo International Trade Fair, held each year during the last week of August and the first week of September, is an important opportunity to reach both the Mozambican and the regional markets. In 1988, the U.S. commercial exhibit included displays by eight U.S. firms, three of which sent representatives. The exhibit was seen by numerous purchasing officials and governmental decision makers. Companies may obtain information on participation in the fair by contacting the Regional Export Development Office (Middle East-Africa), Room H1510, U.S. Department of Commerce, Washington, D.C. 20230. Alternatively, firms many contact the commercial officer of the U.S. Embassy in Maputo, at Avenida Kenneth Kaunda 193, telex 6-143 AM EM MO, for assistance in fair participation and for general marketing assistance.